The Case for a Zero for Zero Sugar Policy in the United States

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Foreword

Since the 1980s, U.S. sugar policy has been a hotly debated issue, pitting two formidable lobbies against one another – sugar producers and large food manufacturers. U.S. sugar policy operates differently than other crops, which utilize a revenue support structure of subsidy checks that kick in when prices fall. U.S. sugar policy is a supply management system that consists of protective tariffs to keep foreign sugar at bay and domestic quotas that limit how much U.S. producers can sell domestically. Because there are no subsidy checks, it is by far the cheapest major commodity program for taxpayers. But, because of the protections in place, major buyers of sugar have historically paid an elevated price, relative to the so-called world market price, which is thinly traded and highly volatile due to subsidization.

New market forces have surfaced in recent years that may have forever altered the debate: First, the U.S. cannot limit sugar from Mexico, which can now ship unlimited quantities once NAFTA took full effect on January 1, 2008. This has created unsustainable oversupplies that could lead to artificially low prices and eventually taxpayer cost. Second, Brazil has seized control of fifty percent of global exports using decades of heavy subsidization and now wields price-setting powers on the global market, as seen by extremely volatile prices since 2008.

This paper examines the current points being made in favor of and against U.S. sugar policy, and possible points of compromise as the aforementioned new market forces exert pressure on consumers and producers alike.

The Pro-Sugar Policy Position

The 21st century brought about significant change in the way that the United States functions as a world power and a competitor in the growing globalized market. With 11.8 million Americans unemployed (July 5, 2013 BLS Report) and a national debt of over $16.7 trillion (July 10, 2013 U.S. Treasury Report), the United States has struggled to resist losing its edge as a contributor to the global market. American small business owners are engaging with foreign markets, while multinational corporations offer hundreds of thousands of jobs offshore. Subsequently, prices for producing goods, like sugar, domestically in the United States are higher and hinder the ability of farmers at home to compete with subsidized markets abroad.

This reality is exacerbated in sugar's case because most sugar is produced in developing countries with lower taxes, lower wages and lower regulatory burdens. In addition, subsidization runs so rampant in sugar production that global sugar prices have routinely run well below the world average cost of producing sugar. Some economists have referred to the world sugar market as a dump market because of the heavy subsidization that enables sugar to trade well below production costs.

According to recent studies, U.S. sugar producers have production costs that are lower than world averages but the price suppressing effect caused by global subsidization makes U.S. sugar policy necessary. This safety net cost taxpayers $0 from 2002-2012, according to Congressional Budget Office data. Under the policy, U.S. sugar prices have remained essentially flat, with a pound of refined sugar costing the same today as it did in the 1980s, as reported by the U.S. Department of Agriculture. U.S sugar prices have been well above the world price in most years, though U.S. and world sugar prices have recently converged.

According to a recent study by University of Maryland Professor Alexander Triantis, prices of sweetened products (for example candy bars, cookies and cakes) have not remained stagnant in conjunction with U.S. sugar prices but have rapidly increased, as has the profitability of sugar-using industries. The fact that food product prices do not track closely with sugar prices is not surprising since sugar constitutes a small percentage of a product's overall price.

There is a misconception among Americans, that twenty-two percent of a candy bar's cost is sugar. In fact, the percentage is roughly two percent. The American Sugar

Alliance has found that since 2010, candy bar prices are up five percent, as well as cereal and baked goods, up nine percent, and ice cream, up twelve percent. Conversely, sugar prices have actually fallen by more than fifty percent since 2010.

Food manufacturers are pouring millions of dollars into lobbying campaigns to deflate U.S. prices further. For years, these companies advocated the complete repeal of U.S. sugar policy and dependence on foreign production. Problems following Hurricanes Katrina and Rita with obtaining high-quality foreign sugar led to an evolution of policy demands. In 2006, food manufacturers proposed sending U.S. sugar farmers subsidy checks to cushion the inevitable price fall associated with tariff removal. That proposal was estimated to cost taxpayers $1.3 billion a year and was therefore never enacted. In 2013, food manufactures are instead looking to impose mandates on the USDA to keep the market oversupplied with foreign sugar, essentially capping prices at, or below, current levels.

Sugar producers argue that this new proposal would eventually kill the U.S. policy, drive them out of business and cede the U.S. market to subsidized foreign producers. Sugar production in the United States supports 142,000 jobs, both directly and indirectly, and without sugar policy, these jobs would be in jeopardy because heavily subsidized sugar from Brazil and elsewhere would flood the U.S. market and drive U.S. producers out of business.

The food manufacturers' position, sugar producers contend, is tantamount to unilateral disarmament – that is, it destroys the domestic industry while rewarding the most heavily subsidized foreign producers.

The Anti Sugar Policy Position

Opponents of current sugar policy in the U.S., namely manufacturers of highly sweetened products, argue that sugar policy is a protectionist relic of the past that is in need of reform. They point to USDA data that indicates U.S. prices rose drastically under the 2008 Farm Bill, which handcuffed the USDA from dealing with supply shortages. This harmed small businesses and gouged U.S. grocery shoppers. Sugar policy is essentially a tax on American consumers and must be addressed to help spur the economy. Anti sugar policy proponents also point to a GAO Report that indicates U.S. sugar policy historically has kept prices higher than around the globe, which, according to a Department of Commerce study, has led to U.S. food manufacturers relocating in search of cheaper sugar and thus, job losses in the U.S. Yet, during recent Congressional debate, sugar was the only commodity to escape reform in the 2013 Farm Bill.

Reforming sugar policy would help bring U.S. prices in line with global averages and would force U.S. producers to compete in a less protected market, just as food manufactures must. They posit that a more free-market approach and subsequent drop in U.S. sugar prices would not result in the widespread loss of sugar-related jobs, which, according to official government data, represent far fewer than the 142,000 jobs the sugar industry estimates. Job loss would further be minimized due to the seasonal nature of the sugar industry. Conversely, reform would lead to job creation in the food manufacturing sector, which is already more vibrant and geographically significant than sugar.

Proponents of reform argue that sugar is a small industry, and according to the Department of Commerce, in its current form it costs more U.S. jobs than it helps protect. They point to an Iowa State University study that concludes that eliminating U.S. sugar policy will help small businesses expand in the U.S. and add jobs.

In sum, although the U.S is the leading importer of sugar, it is doing more to harm the free market than help by setting unfair restrictions on trade and leading to higher prices domestically. In order for business to function as intended and reflect basic principles of supply and demand, barriers to the U.S. market should be removed and all should compete on equal footing.

The Common Ground Held by the Pro and Anti Sugar Positions

While the above discussion may lead one to conclude that the divide between pro and anti sugar policy proponents is too large to overcome, there is clearly common ground that both sides of the debate publicly agree on. Both sides have publicly embraced the concept of a free market. A true free market could eliminate U.S. protectionist policies, thus helping consumers, and ensure a strong domestic supply for years to come. Both sides believe that subsidies are detrimental to the sugar trade market. And certainly both sides agree that domestic production is important to ensuring food safety and high quality standards.

Make no mistake, candy companies would rather buy sugar domestically, if the prices were right, and therein lies the issue. These companies are not inclined to purchase sugar from the U.S market because historically U.S. prices have been as much as double global prices. Of course, domestic sugar prices are significantly higher than the world price in virtually any country with a desire to buffer its sugar industry from foreign subsidized sugar.

But the pro and anti sugar policy sides disagree on how to accomplish long-term viability of U.S. producers. Producers largely want to keep protectionist policies – the status quo, and that position is becoming harder to maintain amid today's market forces. Opponents want cheaper sugar, whether that means letting more subsidized foreign sugar into the U.S. market or having taxpayers subsidize U.S. production (a proposal they made in 2006 during the Farm Bill debate). Both stances reflect unlikely solutions that will only exacerbate political squabbling.

The creation of a unified sugar policy is dependent on its ability to limit the scope of government intervention over sugar cane and sugar beet farmers, while subsequently keeping costs low for candy companies. The true free market approach, the "zero for zero" sugar policy model, that is currently being promoted by American Conservative Union and championed by U.S. Congressman Ted Yoho (R-Fla.) and others is a logical step. Under this approach U.S. officials would push for zero subsidies abroad while using the promise of zero subsidies at home as incentive. As proposed, a zero for zero sugar policy would lift restrictions and tariffs on trade between all players in the global sugar market and would target market-distorting policies, including direct and indirect subsidies. Furthermore, leveling the playing field would be advantageous for consumers, the candy industry and sugar farmers, as all parties would be paying lower prices with less government oversight.

The Results of Sugar Policy Reform in the EU - A Warning for the U.S.

The alternative, simply weakening U.S. policy without demanding reforms abroad, holds serious consequences, as the European Union has proven. In the paper published in August of 2012, "Lessons from the 2006 EU Sugar Regime Reform" by Patrick H. Chatenay of the United Kingdom, the author lays out the post-reform realities of sugar policy in Europe and the UK.

Prior to 2006, the free market reformers in the EU were making much the same arguments we see today in the U.S. as Congress considers the latest Farm Bill. These advocates believe it would be best to open the American sugar market to foreign suppliers and let "the market" decide where prices should settle and where supplies should come from. By offering open market access to many foreign sugar producers, the U.S., like the EU in 2006, would aim to lower domestic prices significantly, improve the competitiveness of its food processing industries, moderate prices for the end-consumer and still enjoy a stable, safe supply of this essential ingredient. However, several truths have emerged since the 2006 reforms in the EU, and each is relevant to the state of debate of U.S. sugar policy in 2013.

First, it has become clear that the liberalization of the market fosters supply uncertainty and price instability. After dropping twenty-two percent, bulk refined sugar prices in Europe are now some ten percent above what they were before the reform and since the end of 2010, the EU sugar market has exhibited high and volatile prices, and a shortage of supplies mirroring world market gyrations. The EU now understands that the intrinsically unstable world market is a poor model by which to set a proper sugar policy, as it remains the outlet for heavily subsidized production from numerous countries such as Brazil, where half its sugarcane is sold onto government-controlled markets.

Second, it is clear that dramatic social costs are associated to the resulting lower profit margins and to reduce domestic production. In the EU since the 2006 reforms, over 80 mills have closed, directly causing 120,000 jobs to be lost, along with unsalvageable damage to the farming communities involved. Five EU member countries have given up sugar production entirely; five others now produce less than half of previous output levels.

Third, the current reality relative to fiscal policy is that, while the old EU sugar policy carried minimal cost to the general taxpayer, the post-reform sugar policy is costing taxpayers about $1.6 billion a year as grower support is paid through federal government budget-financed farm payments.

And finally, the Chatenay study clearly lays out evidence that current data does not support the assumption that lower sugar prices have been transferred to the end consumer. The user industries and the retailers have pocketed the price drop. Even the European Court of Auditors concludes so after examining studies commissioned by the EU.

So essentially, the 2006 EU Sugar Regime reform implemented many of the ideas now being promoted by opponents of current U.S. sugar policy. At considerable cost to stakeholders and without any measurable benefit to the consumer, the EU has put at risk the safety of its supply of sugar. By letting imports determine the ultimate availability of sugar, the EU has lost control over its supply of this essential food ingredient. With preferential imports no longer subject to quantitative controls, the domestic EU market is subject to world market uncertainties. The EU food market now depends heavily on the world market where price and supply instability are the modern reality. At a time of scarce U.S. government finances, is it important to note that the EU sugar policy went from being budget neutral to costing hundreds of millions to the public purse. Lower domestic producer prices have caused income transfer away from farmers and developing countries towards food processing companies without any measurable effect on consumer prices, employment or processed food exports.

Though increased efficiency of the EU sugar industry was achieved, it came at a high social cost, with additional industry concentration, and sugar industries in developing countries have suffered from the lack of certainty offered by a less predictable EU market. Chatenay's study concludes firmly that the 2006 EU sugar policy reform carries warnings, which U.S. policymakers should heed when contemplating how best to improve U.S. sugar policy.

The Case for a Zero for Zero Sugar Policy in the United States

In attempting to reform and improve sugar policy in the United States, it cannot be done unilaterally, as the EU lesson proved. The zero for zero approach to sugar policy holds an as yet untried avenue that could possibly break the stalemate between the pro and anti sugar policy groups.

Consider that there are more than 100 sugar producing countries worldwide, and there are also basically 100 different sugar policies, each of which includes various forms of government intervention. With Brazil controlling half of the world's sugar export market through essentially complete government subsidization, any worldwide free market approach to sugar policy must include their participation. Yet Brazil's latest federal budget includes higher subsidies for their sugar industry than last year, and multiple bailout packages have been announced to aid a struggling cane ethanol sector. For perspective, the OPEC's Saudi Arabia only control nineteen percent of the world's crude oil exports, so Brazil's muscle in world sugar markets is clearly powerful. Add Mexico to the mix, where its government owns twenty percent of their domestic sugar industry and is allowed to dump surplus sugar onto U.S. markets through loopholes in our NAFTA agreement with them. It becomes immediately clear that the U.S. cannot unilaterally create a worldwide free and fair trade zone unless the other major sugar producing countries address and ultimately eliminate their sugar subsidies.

Even though the United States is the fifth largest sugar producer in the world, consuming 11-12 million tons annually, only 8-9 million tons of that demand is satisfied by U.S. sugar growers with around thirty percent of our own demand being satisfied by imported sugar. Our beet and cane sugar growers are among the most efficient in the world, maintaining thousands of industry related jobs with no subsidy checks and thus little to no cost to the U.S. taxpayers. So it makes little sense to buy sugar on the world market and transport it here unless imported sugar prices are artificially low. Current trade deals have led to subsidized foreign sugar flowing into America and it has created all-time high sugar surpluses in the U.S. In fact, there is enough surplus for every man, woman, and child to have 14 more pounds of sugar a year on top of what they already consume. This sugar glut has eroded prices our sugar growers receive to low levels, around 19 cents per pound versus around 22 cents per pound for raw sugar in 1983. While consumer prices have not reflected the lower prices, does the U.S. really want to give foreign countries control over this essential food supply? If a free market approach rewards the best and most efficient business people and not the most heavily subsidized producer, why wouldn't both pro and anti sugar policy proponents want a solution that could stabilize domestic and ultimately world market sugar prices? Furthermore, we cannot repeat the EU reform disaster where prices jumped after sugar policy was unilaterally abandoned.

So what is the next step to make the zero for zero sugar policy a reality? Again, the approach is basically to eliminate our U.S. sugar policy once Brazil, Mexico, and other foreign sugar producers address and begin to eliminate their heavy subsidies to their sugar industries. The President and current administration would find it nearly impossible to move a zero for zero policy through bilateral trade agreements considering the number of countries that subsidize. Furthermore, bilateral and regional trade agreements deal solely with market-access measures and leave domestic support programs alone – better to be addressed in a multilateral context.
Therefore, a more likely approach to more directly address the problem is having the administration work through the World Trade Organization. The WTO is unquestionably the only entity that can deal with all sugar subsidies in all countries at the same time. And if Brazil or other top producers refuse to participate via WTO pressure, the existing tariffs on foreign subsidized sugar imported to the U.S. market should remain in place, although this option is clearly not the preferred approach.

At a minimum, the zero for zero approach could help the pro and anti sugar policy coalitions come together and focus on common ground. When both sides agree that sugar subsidies exist worldwide and that sugar subsidies are a bad thing for a number of reasons, this approach could well be an answer to bring true free and fair trade about. If Brazil and the others would stop subsidizing their sugar industries, the U.S. could eliminate current sugar policy. With governments worldwide out of sugar markets altogether, it doesn't matter which side of U.S. sugar policy you land. Government out of markets creates free markets, and free markets lead to free and fair markets, and that, in the final analysis, is where world sugar needs to be.

About the Author

Dr. Mark Hartley is a Professor of Business and Holder of the Institute for Supply Management - Carolinas/Virginia Endowed Chair in Supply Chain Management in the College of Charleston's School of Business. He has taught courses in Purchasing and Supply Management, Operations Management, and Business Statistics for the past 28 years at the College. Dr. Hartley has published over 100 articles covering a wide variety of topics focusing on business operations in refereed academic journals, conference proceedings and professional trade publications, and is a frequent speaker and contributor to groups such as the Institute for Supply Management and the Decision Sciences Institute. He is a Member of the South Carolina Procurement Review Panel, served on the Governor's Commission on Management, Accountability, and Performance (MAP Commission), and later as Chairman of Charleston County's MAP Commission.